Slow the flow?

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State officials say there doesn't seem to be an appetite to modify laws that deal with the "waste" of oil and gas to protect public revenues from a regional price glut.

Wyoming stands to lose about $470 million this year in unrealized severance and ad valorem tax revenues and royalties from natural gas due to regionally discounted wholesale prices, according to figures presented by the Wyoming Department of Revenue.

The recurring "price differential" is a symptom of natural gas production outpacing the development of pipeline export capacity.

The Wyoming Oil and Gas Conservation Commission is charged with protecting against the physical waste of oil and natural gas. The definition of "waste" includes "the production of oil or gas in excess of (I) transportation or storage facilities," according to state law.

In contrast, another state law says, "it is not the intent to authorize the commission or the supervisor to prorate or distribute the production of oil or gas among the fields in Wyoming on the basis of market demand."

OGCC supervisor Don Likwartz said even if the state wanted to restrict production to protect public revenue, actually doing so presents numerous legal and logistical challenges.

One major problem with proration is that restricting production would have an unequal impact on companies, depending on their size.

For example, Questar Exploration and Production voluntarily shut in a net volume of 1 billion cubic feet of its unhedged Rockies production in June due to low prices in the restricted transportation environment, according to the company's second quarter 2007 report.

Questar is a fully integrated corporation with production, processing, transportation, storage, marketing and distribution subsidiaries. Much of Questar's natural gas production is from deep formations that allow for some opportunity to dial different rates of production.

Small Mom and Pop independents in the Powder River Basin's coal-bed methane fields simply do not have the economic scale to temporarily cut even 25 percent of their revenue.

In addition, the production of coal-bed methane requires that hydrostatic pressure in coal formations be reduced. If wells are shut in, water can flow back into the production zone, requiring months of water discharge when the producer wants to resume production.

"If you shut in a small producer, that's a much larger impact than on a large producer," Likwartz said.

Where it's been done

Likwartz said state and industry officials discussed proration in 1999 and 2003 under the same pricing and public revenue concerns. They determined that not every operator had the physical ability to restrict production, and the state feared interference with private contracts and correlative rights.

Several states, including Oklahoma, Texas and New Mexico, have prorated, or restricted, the volume of natural gas production. The purpose is to avoid oversupplying demand or available transportation to markets, which drives the value of the commodity downward.

To prorate gas production, the state would allow wells to flow at only a percentage of full production capacity. For example, the current prorate for natural gas wells in Oklahoma is 65 percent, according to the Oklahoma Corporation Commission's oil and gas conservation division.

That means a well that can flow 1 million cubic feet per day must be restricted to a maximum of 650 thousand cubic feet per day.

Duncan Woodliff, manager of production proration at Oklahoma's oil and gas commission, said natural gas producers struggled with the same issues in his state, particularly in the 1990s. Rather than set different proration percentages for large and small producers, Oklahoma set one percentage for the entire industry.

"Independents felt they were being squeezed out," Woodliff said.

He said much of Oklahoma's natural gas production is in maturity now, so proration is much less controversial. Wyoming, on the other hand, is projected to again suffer severely depressed wholesale natural gas prices by 2010, if production continues to outpace additional pipeline capacity.

No state fix

It appears Wyoming will maintain its course of "encouraging" speedier investment in interstate natural gas pipelines through the work of the Wyoming Pipeline Authority.

Although the authority has $3 billion in bonding authority to help finance pipelines that benefit Wyoming's revenue from the commodity, the group says it doesn't have tax-exempt status with its bonding, and that essentially negates its effectiveness.

Rep. Tom Lockhart, R-Casper, said it's unlikely that a proposed severance tax break intended to speed up pipeline investment will survive until the beginning of the 2008 legislative session.

And Gov. Dave Freudenthal remains unenthusiastic toward either proration or a severance tax break.

"That authority (proration) does not exist," Freudenthal recently told the Star-Tribune via e-mail. "We raised the issue earlier and it was not well-received by the legislature."

Freudenthal said several Supreme Court cases have limited the OGCC's "waste" authority to just physical waste.

"That's just the nature of our statute," Freudenthal said.

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